

# The Politics of India's Special Economic Zones

Rob Jenkins



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# Overview

India's Special Economic Zone Act, 2005 received the President's assent on June 23, 2005. Well before the detailed regulations that would govern its implementation came into force in February 2006, various government agencies and private-sector actors had begun responding to the Act's provisions. As of this writing (in August 2007), very little actual construction in those areas officially designated as Special Economic Zones (SEZs) has taken place, and the policy's economic and political effects are still a matter of conjecture.

Even so, there is more than two years of fairly robust policy and implementation history to examine; more than seven years if we include the precursor measures contained within the Exim Policy introduced in 2000. Policy regimes have been formulated in various states pursuant to the central SEZ Act, and these (as well as the Government of India's own SEZ guidelines) have been revised in several respects on a number of occasions. Moreover, 'implementation' (in the form of approvals for the creation of SEZs) has moved forward rapidly.

This paper assesses the political dynamics that have arisen in the wake of the Act's passage. Its larger objective is to determine what these might reveal about the politics of economic reform in India more broadly.

There are inherent dangers in using a single policy domain to derive generalizations about processes of much broader scope. This is especially true of a policy still in its infancy. On the other hand, if ever a single policy initiative were capable of serving as a microcosm for the politics of reform it would be India's SEZ Act, which intentionally draws within its ambit such diverse issues as investment (domestic and foreign), trade, taxation, industrial relations, land-use and land reform, environmental sustainability, and others of an even

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more specialized nature. The Act also affects the policy environment facing state governments; indeed, it requires their active involvement to achieve its objectives. There are implications for the functioning of India's system of local government as well.

The political actors concerned are similarly diverse, including almost all political parties, a huge range of business interests and associations (each concerned with the broad policy framework, and many with an intense interest in rules applicable to their sector), bureaucratic actors with turf to protect, and a staggering array of movement groups spread throughout India. Many of the issues involved in implementing the SEZ policy lend themselves to litigation that will have strong political repercussions, especially where these involve land and taxation. Some cases are likely to be of constitutional significance.

Such a multifaceted process — especially one in which the policy regime itself as well as the economic response and political reactions are still a work in progress — militates against the formulation of generalizable findings. Nevertheless, the story of India's SEZ policy to date would seem to hold at least three important lessons.

First, in seeking to manage the process by which the SEZ policy has been introduced, India's governing elites — indeed its policymaking establishment more generally, which extends beyond those in positions of direct or indirect state authority — have run up against the limits of what can be achieved by practicing 'reform by stealth', or by seeking to insulate policymaking from the effects of 'mass politics'.

Second, the political dilemmas that have emerged in the process of trying to implement the SEZ policy highlight an important structural weakness of India's political system at this stage in the process of India's economic transformation: the increasing inability of the state to broker accommodations that would advance its preferred policy objectives. This is largely a result of pervasive corruption and a recent history littered with broken promises — both of which, it is worth noting, were integral to the process of reforming by stealth.

Third, the SEZ policy is more than just another case of businesses seeking to avoid high levels of taxation or to evade onerous regulation. SEZs represent a desire by both political elites and those who aspire to middle-class status to, in a sense, secede from the rest of India — to, in the language of this

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conference's framework, escape the consequences of India's recent 'democratic upsurge.' In the eyes of many social elites and middle-class aspirants, the political ascendancy of historically oppressed groups threatens to sabotage the dream of a more prosperous, efficient, and powerful India. That SEZs might offer a way of permitting the inhabitants of this upwardly mobile India to pursue this dream, *without the need to emigrate abroad*, while simultaneously creating enclaves within which foreign economic influence can be quarantined before spreading to the rest of India, has proven equally appealing to the political wing of India's Hindu nationalist movement.

The paper is organized as follows: Section II overviews the SEZ concept and the policy decisions through which it has taken root in India; Section III outlines the political logic underlying SEZ reform, including how best it might be viewed in the context of existing theories of how India's reformers have contended with the constraints imposed by democracy; Section IV examines the forms of opposition to which the SEZ policy has given rise; Section V summarizes the government's response; Section VI concludes by elaborating on the three propositions advanced in this introduction.

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# India's SEZ Policy

An SEZ is a geographic region within a nation-state in which a distinct legal framework provides for more liberal economic policies and governance arrangements than prevail in the country at large, the intent being to stimulate investment, trade, and employment. Roughly 2,500 SEZs exist worldwide, spread across 120 countries.<sup>1</sup> SEZs are, in theory, supposed to attract large volumes of investment by providing world-class infrastructural facilities, a favourable taxation regime, and the benefits of economic clustering. The benefits for the wider economy are, in theory, more exports, particularly in high-value-added sectors, and ultimately an increase in the rate of sustainable economic growth. Employment generation is also often cited as a potential consequence of an SEZ model.

In the Indian context, the new SEZ policy can be thought of as ushering in a third generation of economic reforms: while the first two phases were dominated, respectively, by efforts to liberalize the macro policy environment, and by the creation of institutions for regulating a market economy, phase three has a special emphasis on facilitating a global presence for India's largest private sector firms and rapidly enhancing the physical infrastructure within which such firms operate.<sup>2</sup>

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<sup>1</sup> [www.sethassociates.com/special\\_economic\\_zones.php](http://www.sethassociates.com/special_economic_zones.php)

<sup>2</sup> Second generation reforms is a term sometimes used to denote, in general, all the reform items left over from the first decade or decade and a half of reform. More specifically, it can take on one of three meanings: (1) the politically difficult reforms that have been sidestepped (labour reform, thorough fiscal reform, privatization); (2) reforms that will be more inclusive, reducing the disparities that have given reform an anti-poor image; or (3) reforms to institutions of governance to make the process of continuous policy change more transparent, predictable, and efficient. See Rob Jenkins and Sunil Khilnani (eds), *The Politics of India's Next Generation*

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Though India did not pass an SEZ Act until 2005, it has been experimenting with the concept since the 1960s. The Kandla Export Processing Zone (EPZ) in Gujarat is said to have been the world's first. This was followed in the 1970s by the creation of the Santa Cruz Electronics Export Zone (SEEZ), which in the 1980s was expanded to include gems and jewelry. The 1980s also saw the creation of EPZs in Noida, Chennai, Cochin, and Falta (West Bengal), followed by the Vishakhapatnam EPZ in 1994. Immediately thereafter, also in 1994, the policy was revised to permit (in addition to the central government) state governments, autonomous agencies, and private-sector firms to develop and operate EPZs. A private sector EPZ in Surat was the first to emerge under the 1994 EPZ policy.<sup>3</sup>

But India's push toward a more comprehensive SEZ policy began in earnest following a visit by then-Commerce Minister Murasoli Maran to China in 2000. Hugely impressed by what he had seen in China's SEZs — and by discussions with Chinese officials — Maran acted quickly to initiate a change in India's policy regime. This took the form of new SEZ rules notified in the Commerce Ministry's Export-Import Policy of April 2000. This produced a precursor of what would later become the 2005 SEZ Act. The 2000 Exim Policy converted the existing EPZs into SEZs. The main difference between EPZs and SEZs concerns comprehensiveness. Whereas EPZs can be thought of as industrial estates, SEZs typically contain the fully array of social facilities — housing, hospitals, schools, retail developments — that make up a small city. Moreover, SEZs are designed to operate on the principle of 'self-certification' on tax-exempt transactions, whereas EPZs usually require official attestation. Finally, SEZs tend to be governed by comprehensive legislation, under which far-reaching regulations are authorized, rather than through notifications and orders issued by a range of ministries.

Between 2000 and 2005, when the SEZ Act was passed, only three additional EPZs had been established — in Indore (MP), Manikanchan-Salt Lake (West Bengal), and Jaipur. Several states, however, enacted SEZ legislation or developed policy frameworks within the context of existing legal provisions.

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*of Economic Reforms*, Special Issue of *India Review* (Washington, DC), Vol. 3, No. 2 (November 2004).

<sup>3</sup>Ram Krishna Ranjan, 'Special Economic Zones: Are They Good for the Country?', *CCS Working Paper No. 156*, Centre for Civil Society, New Delhi, 2006.

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These included relatively under-industrialized states such as Uttar Pradesh, which under Chief Minister Mayawati passed the UP Special Economic Zone Act of 2002, and Rajasthan, which enacted rules approved by Chief Minister Ashok Gehlot in November 2002. On the eve of the 2005 SEZ Act's passage, 811 business enterprises were operating inside the boundaries of SEZs country-wide.

The SEZ Act of 2005 — and the policy actions and implementation decisions taken pursuant to the Act — encompass an enormous range of policy domains. Beyond trade and investment, SEZs are an instrument of radical deregulation, infrastructure creation, and changes to the tax regime. The SEZ Act is intended to furnish a single-window process for obtaining the clearances necessary to develop an SEZ. This nevertheless affects a huge assortment of government departments and parastatal entities, many of which are involved in the approval process. Moreover, the tax incentives offered for SEZ developers, as well as businesses intending to operate within SEZs, involve provisions that explicitly alter several other pieces of existing legislation such as the Banking Regulation Act, the Income-Tax Act, the Insurance Act, and the Stamp Duties Act.

For a major piece of economic legislation with such far-reaching implications, the SEZ Act 2005 was passed relatively quickly — just a year after the UPA government's arrival in power. Its drafters built upon and were influenced by earlier policy development work conducted under the previous government, notably the Report of the Steering Group on Foreign Direct Investment, prepared by the Planning Commission in 2002.<sup>4</sup> This report quoted liberally from studies conducted by management consulting firms (such as AT Kearney, the Boston Consulting Group, and McKinsey) about problems faced by foreign investors in India: incorrect information about official procedures, delays in obtaining approvals, ambiguity about environmental regulations, a lack of clarity concerning the competencies of state and central agencies, and so forth. The foreign investment committee's report and other policy documents were inputs into the process by which the SEZ Act 2005 was formulated.

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<sup>4</sup>Government of India, Planning Commission, 'Foreign Investment': Report of the Steering Group on Foreign Direct Investment (New Delhi, August 2002).

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Under the Act, firms operating within SEZs are attracted not only by the provision of dedicated infrastructure, but by a package of tax and non-tax incentives that includes: exemption from export and import duties, excise duties, and central or state sales tax. Businesses receive tax deductions on 100% of profits and gains from exports for the first five years of operation within an SEZ; 50% of profits from exports for the next five years; and up to 50% of profits for a further five years (i.e. up to 15 years after commencing operations) provided that funds are credited to a Special Economic Zone Re-investment Reserve Account, the proceeds of which must be used for approved business activities. The main requirement that firms must meet to receive these benefits is the maintenance of a positive Net Foreign Earning position during each of the tax-assessment periods covered. In addition, firms operating within SEZs need not acquire licenses for importing capital goods or raw materials, and they can start joint ventures with up to 100% FDI without the need for investment approval (except in certain cases, such as armament manufacturing or the production of alcoholic drinks and tobacco products).

SEZs can be developed by state-level public agencies, private promoters, or a mixture of the two. It was foreseen by the architect's India's SEZ policy that private-sector firms would be the main drivers of SEZ creation. Applications for the establishment of an SEZ are, not surprisingly, a complicated affair, involving an array of certifications and various forms of proof of intent and competency. But the approval process takes place via a 'single window,' the Board of Approvals (BoA) within the Ministry of Commerce and Industry. Though in theory it is possible to submit an application directly to the BoA, in practice firms seeking to establish an SEZ choose the option of routing their applications through the state government in whose jurisdiction the SEZ will be located, for without the support of the state government concerned, a proposed SEZ has little chance of becoming reality. The BoA operates under a fairly transparent set of guidelines: the relevant documents are available on the ministry's dedicated SEZ website, though as with other government processes, the prospects for success rely on the applicant's grasp of unwritten rules and mastery of political influence-peddling.<sup>5</sup>

As of August 2007, the BoA had given formal approval to 366 proposals and

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<sup>5</sup><http://sezindia.nic.in/>

'in-principle' clearance to 176 others. Another 268 proposals were 'pending'. Of these, there are about 170 cases on which the response of state governments is awaited.<sup>6</sup>

In addition to the BoA, the SEZ policy stipulates the creation, for each SEZ, of a 'Unit Approval Committee' (UAC), headed by the state appointed civil servant, the Development Commissioner. The UAC, consisting of a mixture of private-sector and government officials (customs authority representatives, for instance) approves the entry of new business units into a particular SEZ and makes determinations on the application of other rules (regarding the location of social facilities, the measurements to be used in determining 'processing area', environmental clearances, and so forth).

In many countries, SEZs are considered a means of solving certain economic shortcomings. SEZs have typically been regarded as part of 'regional development' paradigm emphasizing the benefits of geographic clustering among firms in a particular economic sector. SEZs have been seen, for instance, as a means of facilitating more efficient links between consumer-product manufacturers and their suppliers. The idea has been to promote concentrations of sectoral expertise in order to kickstart entrepreneurial activity within related sectors — that is, to see SEZs as 'regional growth poles' from which an expanding area of economic dynamism would gradually emerge.

Another highly touted benefit of SEZs has been their ability to create the world-class infrastructure that firms require in order to make their operations globally competitive. While governments might be unable to provide high-quality road and rail systems, communication networks, water-supply systems, or electricity production and distribution facilities on a country-wide basis, the state could undertake a program of public-sector investment in a limited number of locations where the economic payoffs would be largest and most immediate. The ability of vibrant centers of innovation and production to catalyze a wider process of economic growth, from which areas beyond the SEZs themselves would benefit, has been the standard justification for concentrating infrastructure investment in certain areas rather than ensuring a more even geographic spread.

To yield the desired economic payoffs, however, SEZs were expected

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<sup>6</sup><http://sezindia.nic.in/HTMLS/approved-sez.htm>, accessed 1 September 2007.

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to operate on a large physical scale. A critical mass of firms was required for the benefits of clustering to manifest themselves. A very large increase in entrepreneurial dynamism was necessary before localized growth would spread to surrounding areas. Infrastructural investments would, similarly, be worthwhile only if they covered a wide enough area.

The Indian approach to SEZs has deviated from this logic to a considerable degree. Its SEZ policy — like India's policies in many other fields — exhibits local features that distinguish it from what is commonly found in other countries. India's SEZ Act is different in at least three key respects from the Chinese 'model', which was said to have inspired Murasoli Maran at the beginning of this decade.

First, and perhaps most importantly, whereas in China it was the public sector that was overwhelmingly responsible for developing the SEZs, in India this task has been assigned to the private sector. Private-sector promoters of SEZs have in many cases partnered with government entities. But by far the greatest share of the investment capital is coming from the private sector.

The second difference between India's SEZ policy and the internationally recognized paradigm for SEZ development is the lack of emphasis in India on using SEZs as a mechanism for promoting under-industrialized areas. India's SEZs are — because of the incentives created by the policy design, and the fact that they are, for the most part, not initiated by government bodies — overwhelmingly located in areas that are already highly developed. Almost half (171) of the 366 SEZs approved as of 31 August 2007 were to be in the vicinity of major cities. Just nine cities — Ahmedabad, Mangalore, Chennai, Delhi, Gurgaon, Hyderabad, Kolkata, Mumbai, and Pune — accounted for 138 of these. This is a far cry from what took place in China.<sup>7</sup> Shenzhen, perhaps the world's most famous SEZ, was located in an industrial backwater. Subsequent SEZs have been sited even farther from China's most developed regions, the explicit aim being to disperse the economic benefits that have allowed parts of China to prosper.

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<sup>7</sup>The four original SEZs in China were Shenzhen, Shantou, Zhuhai, and Xiamen. For accessible overviews of the Chinese experience with SEZs, see George T. Crane, *The Political Economy of China's Special Economic Zones*, (Armonk, NY: M.E. Sharpe, 1990), and YC Jao and CK Leung (eds), *China's Special Economic Zones: Policies, Problems and Prospects* (Hong Kong: Oxford University Press, 1986).

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The third way in which India's SEZs vary from the Chinese model has been in terms of scale. The SEZ Act 2005 specifies extremely low minimum size requirement in order to establish an SEZ. The minimum area requirement for 'multi-product' (i.e., non-sector specific) SEZs is 1000 hectares. Sector-specific SEZs have a minimum area requirement of 100 hectares, with the exception of those devoted to Information Technology and IT-enhanced Services (IT/ITeS), which are permitted to be as small as 10 hectares.<sup>8</sup> Implementation of the Act, in practice, has yielded a proliferation of relatively small SEZs. For instance, Gurgaon — an enclave in Haryana that has more or less been absorbed into greater metropolitan Delhi — has emerged as a major SEZ destination. Ninety percent of the first 50 SEZs approved in the Gurgaon area were sector-specific, and of very small size: 36 in IT/ITES, and three each in biotech, textiles, and gems/jewelry.

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<sup>8</sup>SEZ Authority, Ministry of Commerce & Industry. Government of India. Available at [sezindia.nic.in](http://sezindia.nic.in)

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# Political Constraints and the Hedging of Political Risk

Regardless of one's view of the merits of India's brand of economic reform, or the wisdom of the pacing and sequencing of its various elements, the gradually shift over the past quarter century to a more market-oriented economy, with a larger role for the private sector and much greater openness to the world beyond India, has generated considerable — if fluctuating — political resistance. How opposition has been so successfully managed is a matter of some disagreement. Varshney, for instance, has pointed to the tendency of reformers to avoid taking policy decisions that would impinge on the lives of ordinary Indians; in doing so, they have left the domain of 'mass politics' relatively untouched by liberalization. (In exchange, identity-based mobilization — and the shifting political coalitions to which it has given rise — has helped to insulate policymaking from the vagaries of mass politics.)<sup>9</sup> Jenkins, while granting the less-than-aggressive nature of India's reform efforts in many respects, has stressed the capacity of India's democratic institutions, and the politicians and parties that operate within them, to undercut key sources of resistance — by fragmenting opposition to reforms, by shifting blame and political burdens away from those who take key reform decisions, by sequencing policy measures in ways that forestall political confrontations until more propitious circumstances prevail, by brokering agreements between contending interests, and by efficiently steering compensation to the most potentially disruptive

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<sup>9</sup>Ashutosh Varshney, 'Mass Politics or Elite Politics? India's Economic Reforms in Comparative Perspective', in Jeffrey D. Sachs, Ashutosh Varshney, and Nirupam Bajpai (eds), *India in the Era of Economic Reforms* (New Delhi: Oxford University Press, 1999).

groups among reform's 'losers'.<sup>10</sup> In other words, even if reform is not all it's been cracked up to be, and even if reformers benefited from the salience of non-economic cleavages which prevented anti-reform groups from coalescing into an effective electoral bloc, India's liberalizers still faced an uphill task and have been surprisingly agile in achieving the results they have to date.

How, then, can we interpret the introduction of the SEZ policy in light of the political dynamics that have attended India's reform trajectory since 1991 — or indeed since 1980, or 1984, or whichever of the watershed dates is used to mark the onset of liberalization? <sup>11</sup> Does the ardent pursuit of a far-reaching SEZ policy — in which catering to the global market and welcoming foreign investors are highly visible features — signal a retreat from the political caution that, by most accounts, has characterized India's reform process to date? Has India's accelerated growth rate of recent years — or the disarray in which opponents of liberalization have found themselves after a decade and a half of creeping marketization and globalization — emboldened reformers to take greater political risks? Because the SEZ Act contains provisions with an impact on so many aspects of economic policy; because its implementation requires the involvement of so many government departments and levels of the political system; because it touches on sensitive political issues (such as land-ownership) — for these and other reasons it is the kind of legislation that one would have expected any democratic government, but particularly one with a reputation for political timidity, to be highly wary of championing.

Upon further reflection, however, it becomes apparent that the very nature of the SEZ policy requires us to ask the opposite question as well: is not the defining characteristic of the SEZ policy — the limit of its geographic extent — an indication of the continued risk-aversion of India's reformers? If the Government of India were so confident of its ability to press ahead with a bold and comprehensive programme of liberalizing measures, why have not, for instance, the floodgates been opened to foreign investment in the country at large, rather than in a few small enclaves? If the efficient operation of an in-

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<sup>10</sup>Rob Jenkins, *Democratic Politics and Economic Reform in India* (Cambridge: Cambridge University Press, 1999).

<sup>11</sup>For the advantages of seeing 1980 as the crucial watershed, see Atul Kohli, 'Politics of Economic Growth in India,' — published in two parts in *Economic and Political Weekly*, 1 April and 8 April 2006.

dustrializing society requires the firm hand of a 'Development Commissioner', under whose authority a huge number key decisions could be rendered — as is envisaged for SEZs — why not introduce the governance reforms contained within the SEZ Act to *all* of India? If firms operating in SEZs, and the residents who will enjoy their social amenities, are so certain to benefit from streamlined regulatory procedures, is not the government's unwillingness to cut red tape with similar zeal in the rest of India an admission that it is prevented from doing so by the realities of democratic politics?

Paradoxically, the answer to these two sets of seemingly contradictory questions is — with important qualifications — 'yes'. The SEZ policy reflects both the full-throttle reformist ambition of liberalizers at the apex of the political system (and not a few of those operating at the state level and below) as well as the very real and stubbornly persistent constraints that a liberal political system imposes. This is, in fact, just one of the paradoxes thrown up by India's SEZ policy. For instance, while SEZs are geared towards attracting foreign investment, by far the largest share of political protest has concerned the actions of domestic firms seeking to develop them. Or consider the fact that, while the initial development of an SEZ may take place through a single-window approval process, the actual governance of an SEZ, once up and running, is likely to furnish a wide array of state officials huge scope for discretionary decision-making.

The fact is that, even if SEZs have in practice brought economic reform directly into the arena of mass politics — most notably, by permitting state-facilitated industrialization to intrude directly into the agrarian sector through the process of land acquisition (as opposed to indirectly through shifts in the terms of trade) — the process has been one in which established techniques of political management have been clearly in evidence. Even the arrival of the first round of SEZ policy through the backdoor of the Exim Policy was consistent with the stealthy tactics through which earlier rounds of reform have been introduced in India.

SEZs in fact represent a relatively attractive way, politically speaking, of introducing reforms that the Government of India (and state governments) have otherwise felt politically constrained from undertaking. To the extent that they create new industrial townships, for instance, the SEZ policy is a convenient means of overcoming the huge obstacles (bureaucratic and legal,

but ultimately political) to urban redevelopment. Barriers range from the diversity of agencies and authorities with overlapping jurisdictions (each with its own set of entrenched political defenders), to outmoded legislation like the Urban Land Ceiling Act and the Rent Control Act (each of which, again, has proven extremely difficult to revise).<sup>12</sup> Promoting SEZs are also an attractive option given the legal disputes — often traceable to political gridlock — that have tied up so many other brownfield industrial sites. The provisions of the Sick Industrial Companies (Special Provisions) Act 1985 and the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act 2002 make such lands more or less unavailable for industrial development.<sup>13</sup>

To use a different example, should not the SEZ policy be seen as a response to the failure of the Electricity Act 2003 to generate the anticipated flood of new investment in this crucial infrastructure sector? Most of the blame for this failure, it has been argued, is attributable to the refusal of state governments to relinquish control over their State Electricity Boards.<sup>14</sup> SEZ policy thus reflects the constraints on policymakers as well as their striking ambition.

The possibility that the implementation of India's SEZ policy would encounter political opposition was not unanticipated by the politicians and party strategists who weighed the risks and decided to make SEZs a priority on the UPA government's legislative agenda. Despite the potential hazards, pursuing the SEZ policy was considered politically *feasible* by the managers of economic reform for a number of reasons. (This is distinct from why it was considered politically *desirable* in the first place — notably (a) the ability to favour well-funded business interests, and (b) the opportunity to introduce policy changes that were considered too politically risky to undertake on a country-wide basis.)

First, the SEZ policy would be considered of mainly elite interest — it would attract the attention of policy analysts, people concerned with trade and

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<sup>12</sup>A graphic overview of these problems in the context of Mumbai is provided in 'India's Commercial Capital: Maximum City Blues', *The Economist*, 30 August 2007. In the article, Anand Jain, a partner in the Ambani mega-SEZ in Mumbai is quoted as saying: 'Why do they worry about my bloody SEZ? ... Why not have ten SEZs and solve all Mumbai's problems?'

<sup>13</sup>'Starting Trouble', *Frontline*, 29 December 2006.

<sup>14</sup>'SEZ Frenzy', *Economic and Political Weekly*, 30 September 2006, pp. 4095–96.

investment, business associations, and the financial press. Discussion of the various policy questions involved in the establishment of SEZs would, over time, grow highly technical. For instance, debates over the long-term revenue implications of sector-specific SEZ implementation would hinge on the details of complex forecasting models. It was reasonable for the UPA's political strategists to predict that even politically engaged people — let alone the great mass of ordinary citizens — would grow tired of these debates. The policy agenda would move on. More visible events and controversies would come to the forefront. This is to some degree what happened: during the two years following the Act's passage, newspaper headlines, parliamentary maneuvering, and political agitations focused on such hot-button issues as OBC reservations in educational institutions, the remnants of the Bofors case, the Indo-US nuclear cooperation agreement, and so forth. Perhaps, objectively speaking, ordinary people *should* have recognized (and given priority to opposing) the inherently regressive nature of corporate tax 'giveaways' through the SEZ policy, or the cuts in government spending they would imply. But like the Bush administration's tax reformers, the political managers of India's liberalization program were reasonably confident that the issue could be massaged.

Second, strategists in Delhi expected resistance to the SEZ policy to be fragmented — in two senses: it would be (a) *geographically* dispersed; and (b) divided on the *basis* of the opposition. As a geographically limited policy implemented, by definition, in carefully demarcated areas, the most immediately affected constituencies (and therefore the potential sources of political resistance) would be of a localized nature. Those opposed to SEZ implementation in any given location would be isolated within a relatively contained area where the political fallout could be minimized. They might attract sympathy from social activists from surrounding areas, or perhaps elsewhere, but would find it difficult to recruit dedicated allies, whose preoccupations would naturally be with issues of much broader scope. Even if protestors from different SEZ sites within a state could somehow join forces, those from different states would face barriers of distance, language, and political priorities.

Moreover, the *basis* for opposition to the SEZ policy would vary from place to place, from group to group, and between individuals. At the time the draft legislation was being discussed in 2005, it was apparent enough that, while some critics were concerned almost entirely with specific aspects of the policy

(tax concessions that were considered too generous, or too unconditional, or too biased toward certain sectors), others were opposed on broad ideological grounds, seeing in SEZs a Trojan horse for a new wave of liberalizing reforms that would spread to the country at large. Still others were opposed to the timing of the SEZ policy's introduction, insisting that improvement to the conditions facing agriculture should be made before a big push toward industrialization — on land that farmers would be required to sell under indirect duress — was attempted via the SEZ approach.

Faced with such a disunited array of political opponents, the government foresaw the possibility of addressing the complaints of each group individually and serially, picking off discontented constituencies one at a time, as it were. Ideological opponents who considered SEZs further evidence of the government's embrace of 'market fundamentalism' would be neutralized by the UPA's concurrent efforts to tackle the iniquities of liberalization by passing the National Rural Employment Guarantee Act. To those who worried that SEZs would emerge as areas where labour rights and environmental protections were progressively eroded the government could point to its commitment to transparent governance, manifested in its enactment of Right to Information legislation. Critics of the SEZ's policy design — on minimum or maximum area requirements, on the structure of tax concessions, on compensation issues — could be engaged with (or not, depending on how vocal and effective their opposition turned out to) through the process of policy revision.

Third, political strategists in Delhi felt justified in expecting political resistance to be manageable because of the assistance they were likely to receive from state governments in managing the process of policy refinement and implementation. Most state governments, it was clear, would be eager to attract SEZ promoters to their jurisdictions — because they wanted to create jobs and build their economies, and for less public-spirited reasons as well. Political managers in Delhi were confident of the ability of states to arrange accommodations between contending groups. States possessed both skills and incentives to ensure that whatever varieties of political discontent arose would be contained. India's history of accommodative politics has inculcated a fairly widespread belief that where public decisions create 'losers', such groups

could be compensated to the extent that political expediency required.<sup>15</sup> (This belief is consistent with the political assumption of neoliberal policy advocates, who are not unaware of the dislocations policy shifts can cause, but tend to argue that adversely affected interests — or at least a sufficient proportion of their number — can be won over with compensatory adjustments.)<sup>16</sup> After all, interest groups in India are routinely drawn into negotiations over legislative provisions, policy design, institutional structure, administrative rules and so forth. The Indian state's extensive experience at brokering such agreements instilled confidence that accommodations between contending interests (namely, farmers and industrial promoters) could be arranged.

Finally, from the vantage point of political strategists in Delhi — a relatively small group of advisors whose views are coordinated in the PMO, which retains a good deal of decision-making authority — the SEZ policy would be relatively immune from charges that it was copied from the Bretton Woods recipe book. Indeed, India's SEZ policy could be rhetorically positioned *vis a vis* the Chinese economic success story. SEZs were, from 2000 onwards, sold by Maran and others as a necessary weapon in India's struggle to match China's economic might. Whatever its idiosyncrasies, the SEZ Act 2005 was to be portrayed as an adaptation of Chinese methods of economic growth — and as part of an east Asian model more generally. Not surprisingly, state governments too began justifying their SEZ policies in terms of replicating the Chinese model.

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The SEZ policy should, therefore, be seen as an attempt to continue the process of managing India's reforms (and the integration of India into the global economy) in ways that would prevent a hostile and potentially debilitating political backlash. Because the SEZ Act was specifically intended to create enclaves in which the applicable legal regime would diverge from that

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<sup>15</sup>A more recent statement of this view can be found in Aseema Sinha, 'Economic Growth and Political Accommodation', *Journal of Democracy*, vol. 18, no. 2 (April 2007), pp. 41–54.

<sup>16</sup>For a theoretical account of this tendency, situated in a slightly different context, see Sanjay Jain and Sharun W. Mukand, 'Redistributive Promises and the Adoption of Economic Reform', *American Economic Review*, vol. 93, no. 1 (March 2003), pp. 256–264.

<sup>17</sup>This was done explicitly in UP, for instance. The state's Industrial Development Commissioner invoked the Chinese case at the time the UP Special Economic Zone Policy 2006 was launched. 'Special Economic Zones Thrown Open to Private Sector in U.P.', *The Hindu*, 2 August 2006.

## POLITICAL CONSTRAINTS AND THE HEDGING OF POLITICAL RISK

prevailing in the rest of India, its passage was an explicit recognition that it was not politically feasible for the policy measures contained therein to be implemented on a nationwide basis. That the political risk of pursuing fairly radical policies within defined geographic zones was nevertheless considered by India's ruling coalition to reside within manageable bounds points to a belief that the SEZ Act represented a logical extension of the strategy of cautious political management pursued since 1991.

The SEZ policy was, in other words, a hedged bet — demonstrating a recognition of political and institutional constraints, but also a degree of confidence in the state's capacity to extend the boundaries of the possible.



# SEZs as Political Lightning Rods

The passage of India's SEZ Act by parliament, which proceeded with relatively little serious opposition, was not without controversy. Though muted in some respects, criticism of India's SEZ policy partly centered on the deviation of India's approach from the standard (internationally recognized) paradigm, along the lines outlined in Section II, above.

There was of course the usual ideological opposition to what was seen as further entrenchment of a market-friendly (or excessively pro-business) economic framework. This emerged mainly from the left, but also from some remaining *swadeshi* voices in the Sangh Parivar. This was combined, in some instances, with the complaint that India's SEZ approach was not following the standard pattern: if export-oriented enterprise zones had to be created, why could they not be developed by the public sector? The accusation was more polemical than anything else — since such zones were seen as a distraction from more pressing policy concerns in any case — but they provided an opportunity to ask why India's governing elites had so completely lost their faith in the state.

Another complaint centered around the failure of the proposed policy to prioritize the rectification of regional inequalities within and between states. Given the UPA government's purported concern with this problem — not least because it tends to be blamed on, and therefore undermine political support for, liberalization — it seemed fair game to wonder aloud why the incentives provided in the SEZ policy were not being designed as a mechanism to steer investment toward less desirable regions.

Worries about the revenue implications of the SEZ policy were evident from the very beginning of the process. The concerns expressed by the finance

ministry became a central theme of the debate, seized upon by people of almost all political stripes. These continued throughout the implementation phase, and have, if anything, increased in intensity — partly because more sophisticated models for measuring the impact of the tax concessions have been developed, and partly because the scale of the response to the SEZ policy has made the absolute numbers involved so large.

Indeed, one of the most common criticisms of India's SEZ policy has been that its tax-incentive provisions will cause the government to forgo revenue that it can ill-afford to lose. This point has been made, in one form or another, by well-respected economists, including, for instance, former IMF chief economist Raghuram Rajan. While releasing the IMF's *World Economic Outlook* for 2006[<sup>^</sup>/07], Rajan, who is generally careful in his statements and not given to inflated rhetoric, called the tax provisions a 'give away'. His concern was twofold: that the incentives would distort economic activity away from other (Domestic tariff area, DTA) parts of India, and that it would harm India's overall fiscal position.<sup>18</sup>

While Rajan's comments and those of other economists have generally been measured — stressing the timing and precise structure of the tax incentives — the political environment into which these criticisms have been introduced has been sufficiently contentious to ensure that the simplified message — 'tax give away to the rich' — has become a powerful rhetorical weapon for opponents of SEZs and indeed the general direction of India's economic policy.

There are complicating factors, however. In addition to a host of technical measurement issues,<sup>19</sup> there seem to be two points of contention. The first is whether the revenue that is 'foregone' would actually have materialized in the absence of the incentives created. Supporters of the concessions say that without incentives the economic activities (and therefore the taxes thereon) would not take place, so the idea of foregone revenue is notional at best. Had the goods not been produced (as they allegedly would not have been had it not been for the prospect of exports), no tax would have been collected. The

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<sup>18</sup>Andy Mukherjee 'Viewpoint: Trade Zone Hang-ups', *International Herald Tribune*, 3 October

<sup>19</sup>The best discussion of the various considerations involved is found in the work of R Kavita Rao of New Delhi's National Institute of Public Finance and Policy. See 'Special Economic Zones: Gain or Drain?', *Business Standard*, 8 September 2007.

other elements of foregone revenue would derive from potential abuses of SEZ regulations (as with abuses in other export-promotion initiatives) — such as when goods produced allegedly for export are diverted to the Domestic Tariff Area.<sup>20</sup> Critics of the tax concessions say that the 'additional' economic activities are not additional at all: they would have taken place anyway, though possibly in different form, and so would have generated tax receipts that now must indeed be foregone.

A second issue concerns the relationship between the tax concessions in the SEZ policy and those available under other (export and non-export-linked) schemes. Supporters of the SEZ tax concessions say that estimates of foregone revenue fail to take note of the fact that much of the revenue is notional due to the likelihood that businesses would have taken advantage of other tax-holiday schemes had the SEZ policy not been in effect. Critics counter that, if true, this negates the argument for regarding SEZ investments as 'new', and thus undercuts claims concerning the size of 'additional' tax-yielding activities created by SEZs. Either way, the SEZ policy does include one provision that other schemes do not, which is the foregone tax on the development of the SEZ itself.

A related charge has been that the wrong sectors are getting favoured. Especially IT/ITeS, which is no longer an infant industry. Of the 366 approved SEZs, 226 are for IT/ITeS. IT/ITeS was doing well already, it has been argued. It grew by 240% between 2004 and 2007, and the sector was receiving huge infusions of foreign investment in any case. And the scope for job creation — another of the SEZ policy's objectives — was limited at best. IT companies were merely shifting into 'mini-SEZs' — IT/ITeS SEZs need only be one-tenth the size of most other product-specific SEZs — as a way of extending tax holidays due to expire in 2009.<sup>21</sup>

Among the criticisms of India's SEZ policy, one line of complaint acquired a particular resonance in the debate surrounding the passage of the Act, and has continued to serve as a potent mobilizing platform. Social activists and public-interest lawyers have voiced deep apprehension that the mode of gov-

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<sup>20</sup> For an explanation of some of these considerations, see Sukumar Mukhopadhyay, 'Giving a Dog a Bad Name', *Business Standard*, 25 August 2007.

<sup>21</sup> Swaminathan S Anklesaria Aiyar, 'Killing the Best, Aiding the worst SEZs', *Economic Times*, 11 April 2007.

ernance within SEZs, once these are established, would run counter to the principles of democracy. This has been expressed in various catchphrases — SEZ promoters as the ‘new landlord class’; the emergence of ‘neo-zamindari’ forms of governance; and the rise of ‘corporate colonial rule.’<sup>22</sup> Many critics of SEZs consider them a species of corporate entity designed precisely to slip between the cracks of government regulation. SEZs are regarded as locations in which the constraints of fully representative government would not apply. Those who reside and/or work within SEZs, it is feared, might find themselves in a legal grey area in which neither the voice of the majority nor the rights of the minority would receive due recognition. Burman, for instance, points to the lack of clarity surrounding ‘the legal regime affecting the functioning of an enterprise working within the SEZ.’<sup>23</sup>

The creation of distinct zones of governance is not entirely new, there being distinctions between the forms of government in municipalities and rural areas, between notified tribal areas and other locations, and between industrial townships, such as the 100-year-old Tata-run Jamshedpur complex, and other state jurisdictions. Serious shortcomings have, in fact, been highlighted in the governance of even smaller-scale industrial sites.<sup>24</sup> But never has the creation of distinct regulatory spaces taken place on such a large scale, in such a short period of time, and with the expenditure of such vast resources. As Burman put it, the SEZ Act 2005 provides enormous ‘latitude to the concerned governments to regulate, or more importantly, not regulate the operation of companies within an SEZ.’<sup>25</sup> Burman looks at this from the perspective of corporate governance, or how firms themselves are governed — a very important issue in this case, since it is firms, to a large extent, that will be responsible for governing extensive areas in which millions of people will have their residences and conduct their social lives (educating their children,

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<sup>22</sup>All three terms appeared in a petition signed by representatives of 37 NGOs and activist groups, entitled ‘Revoke the SEZ Act’, 28 June 2007.

<sup>23</sup>Anirudh Burman, ‘Special Economic Zones: Issues in Corporate Governance’, IDRC Working Paper, February 2007, Ottawa.

<sup>24</sup>See Amita Singh, ‘Accountability in Local Governance: Infrastructure Development in the Industrial Townships of Faridabad and Gurgaon’, in Niraja Gopal Jayal, Amit Prakash and Pradeep K. Sharma (eds), *Local Governance in India: Decentralization and Beyond* (Delhi: Oxford University Press, 2006).

<sup>25</sup>Burman, ‘Special Economic Zones’, p. 5.

consuming products, conducting religious worship, an so forth).

At the heart of these concerns are the structures of public-private decision-making within SEZs. That SEZs are being developed by private-sector firms, which will act as their managing agents, raises huge questions about how the zones will be governed. The role of the Development Commissioner, discussed in Section 11 of the Act, is particularly suspect in the eyes of critics, and even among some supporters, of SEZs. The Development Commissioner is expected to act in consultation with representatives of the state government on certain issues (for instance, certifying compliance with environmental standards), but for most other matters would exercise something like a combination of legislative, executive, and judicial powers as the preeminent member of a board of governors in which the representatives of the SEZ's corporate promoter would have a disproportionate voice. State governments are empowered to delegate to Development Commissioners the powers otherwise conferred upon other state officials.

Press reports and manifestos issued by social activist groups have stoked fears that state governments are seeking to establish permissive legal regimes for SEZs.<sup>26</sup> Section 49 of the Act is a particular source of worry because it specifies the central government's ability to notify the non-applicability of any central act (or rules framed pursuant to any such act) in an individual SEZ or a class of SEZs. The potential uses to which this provision can constitutionally be put — not to mention the willingness to invoke it — is less obvious than it might appear in the more fervid imaginings of some activists. But it is a legitimate worry, not least because of the clear desire of businesses (many of which are seen to have already circumvented the law in the process of establishing SEZs) to gain government assent to a further watering down of what are weakly enforced laws in any case.

Section 23 of the Act is likewise a common point of criticism among opponents of the SEZ policy. This portion of the legislation empowers state governments to establish special courts to adjudicate civil cases. That residents and employees within SEZs will find judicial protections less easy to obtain than they are at present is, again, a legitimate worry. Though Section

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<sup>26</sup>For one of the more balanced accounts, see 'Sovereign States', *Business World*, 13 November 2006.

24 of the Act specifies the right of appeal to a state's High Court, there are reasonable grounds for concern that these and other provisions of the Act, taken collectively, will erode the rights of complainants, or provide a forum within which firms operating inside SEZ bounds would find it convenient to initiate harassment litigation against unions, activist groups, or others.

Potentially more problematic from the perspective of democratic accountability is the seeming exemption of SEZs from the provisions of the 75 th Amendment, which provides for local participation in municipal governance. How and where municipal authorities can or will be established in what in some cases will be newly urbanized areas is not clear. The worry is that the SEZ Act will trump citizen claims to share in the governance of their localities on the basis of constitutionally protected systems of representation. Again, the lack of clarity on this issue has served to incubate a proliferation of scare stories.

In sum, creating parallel zones in which many questions of governance — and not just those related to trade, investment, or production — are subjected to a *sui generis* form of quasi-private management will make India's SEZs, in many respects, 'Special Governance Zones', or SGZs. This term was coined in 1999 by Shang-Jin Wei in a paper presented at a Transparency International (TI) conference on new methods for combating corruption. An SGZ, in Wei's rendering, was to be an enclave within a nation-state where experimental methods for enhancing accountability could be piloted, each zone serving as an 'entry point for a winnable anti-corruption program.'<sup>27</sup> Wei's idea struck many observers at the TI conference as fanciful. But shorn of its emphasis on promoting more accountable governance, a similar idea is in fact being attempted on a much larger scale through India's SEZ policy.

While most of the concerns discussed thus far are speculative in nature, involving problems that might arise once SEZs are up and running, the issue of direct and immediate relevance to the process of establishing SEZs in the first phase of implementation has been land. The issue of land — and particularly of land acquisition — has been instrumental in fusing diverse strands of discontent into a powerful political force. And it is worth noting that many members of the growing chorus of critics on this issue are far from

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<sup>27</sup> [http://www.transparency.org/iacc/9th\\_iacc/papers/day2/ws1/dnld/d2ws1\\_sjwei.pdf](http://www.transparency.org/iacc/9th_iacc/papers/day2/ws1/dnld/d2ws1_sjwei.pdf).

## THE POLITICS OF INDIA'S SPECIAL ECONOMIC ZONES

the usual suspects. One vocal critic is Rahul Bajaj, now a member of the Rajya Sabha, who claims that the SEZ policy is being used by real-estate developers to perpetrate, with government connivance, what amounts to a 'land scam'.<sup>28</sup>

In every state in which a significant number of SEZs have been proposed or approved, local protest groups have arisen around the process of land acquisition. The nature of the opposition has varied from state to state, in part because of variations in the approaches taken by state governments to the question of land availability. But at the core of the protests has been outrage at the abuses of the Land Acquisition Act, and indeed the perceived subversion of the original purpose of eminent domain, which was intended to apply to projects of public importance rather than those involving private profit. There is of course ample scope for state governments to manipulate what constitutes a 'fair-market price' for land that is compulsorily acquired. SEZ promoters, and their political and bureaucratic accomplices, are privy to inside information on the likelihood of regulatory decisions being taken that will affect the future price of the land in question.

On balance it is fair to say that state governments have shown themselves less politically astute than perhaps the architects of the SEZ program in Delhi had hoped. Many state governments have embroiled themselves in serious political controversies. Some clearly expect protests to die down, or do not expect the protests against their actions to harm them politically. Some state-level ruling parties have calculated that their days in office are numbered — apparently the view of members of the Punjab and UP governments in late 2006 and early 2007 — and that it was advisable to milk the SEZ land-acquisition process for all it was worth before leaving power.

A rather more sophisticated calculation is reportedly in play in other cases, where funds raised through kickbacks on land-acquisition are expected to be put to good political use at the next assembly election — on advertising, bribing political middlemen, and purchasing post-poll independents to secure a working majority. In some states — such as Andhra Pradesh — sites have reportedly been chosen with caste calculations kept carefully in mind. Groups

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<sup>28</sup>This view was voiced at a 'Parliamentarians' Forum on Economic Policy Issues', Council for Social Development, 3 May 2007, New Delhi. Bajaj received support from others, including fellow Rajya Sabha member PC Alexander, who (like Bajaj) also advocated setting aside a proportion of the SEZs for Small and Medium-sized Enterprises (SMEs)

that have traditionally voted for the ruling party (or which might conceivably be courted in the next campaign) are said to have been largely spared the pain of compulsory land acquisition, even as others have been disproportionately subjected to tactics of intimidation. This might be thought of as negative clientelism — selectively sparing one's allies in exchange for political support, rather than distributing positive benefits to them.

Even so, as the protests have gained strength and visibility, the ruling coalition in Delhi has found it increasingly difficult to distance itself from the abuses of state governments, particularly those effected by Congress governments. It had been hoped that it would be possible to shift the blame for any complaints onto state governments that, after all, are responsible for land acquisition, and indeed for setting various norms for operationalizing the SEZ policy. But much of the ire is being directed at the centre — partly because it promulgated the SEZ policy in the first place (and so opened the door to abuses); partly because it gives the final approval to projects (and so should be keeping tabs on the sins of state governments); and partly because it is expected to frame effective regulations when patterns of abuse become evident.

The most visible case of grassroots opposition to the process of land acquisition has been in Nandigram, in West Bengal's East Midnapore district, where in March 2007 violence erupted between the police and protestors and 14 people were killed. The Nandigram case has become a *cause célèbre* for anti-SEZ forces across India. There is considerable controversy concerning what took place in Nandigram, with the apportioning of blame following largely party lines. The state-level ruling party's account of events was elaborated in an op-ed piece by CPI-M MP and Polit Bureau member Brinda Karat. Karat acknowledged that mistakes had been made, but accused protestors of being largely from outside the area, motivated by partisan agendas, and supplemented by paid muscle.<sup>29</sup> This version of events has been widely criticized.

But Nandigram is just the tip of a rather larger iceberg. The process of acquiring land for SEZs has sparked protest in almost every case on record. The abuses take a wide variety of forms. Documents presented by Orissa state government representatives at a BoA meeting on 28 September 2006

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<sup>29</sup> Brinda Karat, 'Behind the Events at Nandigram', *The Hindu*, 30 March 2007.



stated the land acquired for SEZs in the state would be only on land that was 'waste' or 'barren', or on land that supported the production of only a single crop.<sup>30</sup> Social activists from Orissa, however, claim that much of the land supports multiple crops. Either way, the resulting controversy created sufficient controversy to convince the promoters of an 1800 hectare SEZ to reduce its size by more than 10 percent.

Protests have erupted whether the SEZ developer in question has acquired land directly from its owners or whether it has relied on state governments to employ the Land Acquisition Act 1894. Many SEZs have combined the two procedures, which has further confused the stories emerging from critics. One large firm, seeking to establish an SEZ near Gurgaon, was alleged to have obtained the collaboration of the Haryana government in pressuring landowners to sell. Though the state government had announced that it would not assist the firm in acquiring land via the Land Acquisition Act, government officials were said to have threatened landowners with the withdrawal of access to infrastructure, and informed landowners that their properties would decline in value once the SEZ eventually came on line due to industrial pollution and reduced availability of water, both of which would occur as a matter of course, but could also, if need be, be engineered by government officials.<sup>31</sup>

Outrage at the use of similarly underhanded tactics has led to protests against several SEZ projects coming up in Maharashtra, one of the major sites for SEZ investment. The Reliance Group's SEZ in Navi Mumbai had attracted not only public protest over land acquisition, but objections from various government entities, including the customs and exports commissioner, the revenue department and the Jawaharlal Nehru Port Trust. The proposed 1900 hectare Videocon SEZ on the eastern outskirts of Pune has led to repeated protests. Local farmers have been agitating under the leadership of several opposition party figures. Their complaint, submitted to the Pune District Collector's office in May 2007, was a familiar one: that members of a prominent political family in the state were using both the official land acquisition process — and informal strong-arm tactics — as part of a personal land grab.

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<sup>30</sup>Government of Orissa, Department of Revenue, 'Declaration of Land Classification for Proposed SEZs in Orissa,' Bhubaneswar, September 2006.

<sup>31</sup>Personal communication with a reporter who covers Gurgaon for the real-estate trade press, 15 June 2007.

Indeed, the tendency for protests against land-acquisition practices to seep from the domain of social activism to that of party politics has provided opposition to the SEZ policy added bite. The 2007 assembly elections in Punjab in 2007 provided an indication of the extent to which SEZ policy could serve as both a symbolic issue and a policy question of material concern to directly affected groups, or those who might fear ending up as such. During the election campaign, Amarinder Singh's Congress government was consistently and vehemently criticized by opposition leader Parkash Singh Badal of the Akali Dal on the 'squeezing' of farmers in the process of acquiring land for SEZs. Farmers were not getting a fair price for their land; some were being coerced into selling; the benefits were destined for real estate developers; industrial development in the state would not be helped. The litany was familiar from other states. The Congress's electoral loss in Punjab cannot be blamed on its approach to SEZ implementation, but the issue provided a symbolic focal point for opponents of what was deemed a callous administration.

The politicization of the land-acquisition protests has in some cases taken on an *intra*-party dimension. In Haryana, a large SEZ planned for Jhajjar generated considerable local opposition, and provided an excuse for disaffected political groups to condemn the (Congress) state government's handling of the issue. In July 2007 a prominent Congress MP from the state, Kuldeep Bishnoi, went from implying the involvement of Sonia Gandhi in what he said was a bribery scandal involving land-acquisition, to outright accusing her of being a 'party to the deal'. Already established as a party rebel, Bishnoi said that the state's chief minister, along with Mrs Gandhi and other senior figures from the national party had all 'received money' from a deal they jointly struck with the SEZ promoter. Bishnoi stated publicly that Mrs. Gandhi had instructed him to stifle his criticisms of the implementation of the SEZ policy.<sup>33</sup> Needless to say these charges, regardless of their veracity, have been quoted by all manner of SEZ critics.

The lack of party-based opposition to the SEZ policy as a whole (as opposed to certain features of the Act, or the manner of its implementation) reflects

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<sup>32</sup>'Farmers Vow Not to Let the State Grab Their Land', India Realty News' 17 May 2007.

<sup>33</sup>'Bishnoi Names Sonia in "Deal" with Mukesh Ambani', UNI, 22 July 2007.

the dispersal of power among India's major parties throughout the federal system. Most parties with a significant parliamentary presence are in power in at least one state, making them prey to the temptations the SEZ policy offers to governing elites at the subnational level. (This is the story, in miniature, of large parts of the politics of economic reform in India.) Implicated in the SEZ policy through their actions as state-level ruling parties, non-UPA parties who might have been expected to find a reason to rail against the SEZ policy have found themselves enjoined by minimal requirements of consistency to keep relatively quiet. This has not constrained them (or indeed UPA parties themselves) from complaining about *implementation* of SEZ policy in states where they sit in opposition.

In Karnataka, the Congress state party unit, currently in opposition, has repeatedly attacked the BJP-JD(S) government on the issue of acquisition of SEZ land in Nandagudi. The Karnataka Congress announced its intention in July 2007 — after the project had been cleared by the Board of Approvals — to submit a memorandum to the BoA in protest against the state government's violations of central implementation guidelines. The Congress president felt obliged to clarify that, naturally, his party was not opposed to the idea of SEZs, but that obtaining land from farmers compulsorily, and at unfairly low prices, could not be countenanced.<sup>34</sup> Karnataka's ruling coalition, not surprisingly, did not want to allow the Congress, which championed the policy in New Delhi, to play both sides of the fence. Soon after the Karnataka Congress began stepping up its mobilization on this issue, the parties that make up the state's ruling coalition announced plans to protest against the UPA government's alleged failure to provide a coherent framework for the implementation of the SEZ policy. The highlighting of inconsistencies in party positions across state lines (and between central and state levels of the political system) is part of a larger trend found throughout India. In Orissa, where the CPI-M is in opposition, its party members level some of the same criticisms made of the CPI-M-led government's SEZ policy in West Bengal. As one state level office-bearer of Orissa's CPI-M put it, '[b]y handing over valuable land to private companies at a throw away price [the Orissa government] will actually end up

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<sup>34</sup>'Karnataka Congress to Submit Memorandum Opposing SEZ', UNI, 14 July 2007.

creating a new generation of landlords.’<sup>35</sup>

Of India’s major parties, the BJP was perhaps the slowest to grasp the political potential of the SEZ-land issue, perhaps in part because it was under the NDA government that the turn toward a new SEZ policy had begun. When the BJP’s leadership finally constituted an intra-party panel to formulate its response to the SEZ policy in October 2006, the impetus came mainly from state-level units, which had been heavily criticized by party activists at the grassroots for not capitalizing on this issue. The party was in power in eight states at that point, and actively pursuing SEZ investment in all of them, an uncomfortable fact that no doubt further slowed its response time (just as the UPA’s political strategists in Delhi had anticipated). M Venkaiah Naidu was appointed by party chief Rajnath Singh to head a panel that would examine the matter.<sup>36</sup> The panel’s tepid findings were that the party had been consistent in its insistence that it was not against the SEZ policy, as such, and was dismayed only at its implementation by the governments of certain states — notably those where the BJP sat in opposition.

In Andhra Pradesh and other states, charges that farmers were being ‘forcibly expelled’ from their land — leveled, in fact, by people with no discernable party loyalties — have nevertheless provided a potent tool for political mobilization. This is partly due to the symbolism involved, but more importantly because of the opportunity that the land-acquisition process provides for opposition parties to zero-in on specific locations — places where the party’s organizational resources can be targeted in pursuit of electoral dividends. The BJP held a strategy session in early August 2007 on how to address the mounting discontent with the Congress state government’s abuse of land-acquisition procedures.<sup>37</sup> It decided that state and local party leaders should hold fact-finding inquiries (in which the quasi-official trappings of hearings and reports and witnesses would feature prominently) to determine whether ‘fertile’ lands had been acquired for SEZs, in contravention of government guidelines, and whether duplicitous tactics had been employed to do so.<sup>38</sup> The geographically focused nature of the SEZ development process — in which

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<sup>35</sup> ‘Rural Resistance’, *Frontline*, 7 October 2007.

<sup>36</sup> UNI, 4 October 2006.

<sup>37</sup> ‘BJP leaders to Visit Proposed SEZ Sites’, *The Hindu*, 6 August 2007.

<sup>38</sup> ‘BJP to Intensify Stir against SEZs’, *The Hindu*, 24 August 2007.

policy grievances are manifested in specific locales — provides a strong incentive for opposition-party machineries to focus their efforts at the grassroots level.

Land issues have been instrumental in forging a broad-based movement opposed to the SEZ policy because they focus attention on reformers' neglect of agriculture and the problems of the rural sector more generally. As P Sainath put it: 'In 60 years we haven't managed — except in three States — to push through any serious land reforms or tenancy reforms. But we can clear a Special Economic Zone (SEZ) in six months.'<sup>39</sup> Ashish Kothari highlights a specific dimension of land-related agriculture policy that is aggravated by the rush to create SEZs. Kothari argues that even a less aggressive form of SEZ land acquisition — in which 'fertile' and 'multi-cropped' land would be spared mutation to industrial and commercial purposes — would still be based on faulty assumptions. As other land-policy analysts — not all of them necessarily radical environmentalists — have pointed out, land that is officially classified as 'wasteland', and therefore available for development, may have other uses for the agrarian economy. Such land may be 'degraded', but should not be written off as 'barren'. Suitably revived, it can serve as grazing land, or can be used for the provision of fodder, or may be important to soil and water conservation to surrounding areas.

Finally, it should be noted that not all states have responded with equal callousness and political ineptitude when it comes to the question of land acquisition for SEZs. As Aseema Sinha's research has demonstrated,<sup>40</sup> India's history of investment policy (both before and after the advent of liberalization) reveals that states vary enormously in how they: (a) respond to central reform initiatives, in terms of both policy frameworks and institutional structures; (b) balance the interests of rural/agrarian and urban/industrial constituencies (not least by blurring the edges between these categories); and (c) manage the political protests (both local resistance and partisan attacks) that arise from their actions.

Different states indeed pursue different policies on a number of SEZ policy

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<sup>39</sup> P Sainath, 'The Decade of Our Discontent', *The Hindu*, 9 August 2007.

<sup>40</sup> Aseema Sinha, *The Regional Roots Of Developmental Politics In India: A Divided Leviathan* (Bloomington, IN: Indiana University Press, 2005).

parameters. Karnataka, for instance, has its own standard for deciding what kind of land can be acquired: according to the Karnataka Industrial Areas Development Board, SEZs are permitted to acquire double-cropped (ie highly fertile) agricultural land, but only 10 percent of the total area may be of this type.<sup>41</sup> The compensation offered to landowners varies considerably across states as well, as does the credibility of governments that offer it (an issue to which we shall return in Section VI of this paper). West Bengal, for instance, pays 30 percent on top of the market rate for lands that are compulsorily acquired, and a much higher payout to sharecroppers than is required by the national legislation. It also has extracted more generous, legally enforceable, promises from SEZ developers for retraining and other facilities. Further detailed research is necessary to specify differences across India's states (and the reasons for these differences) in terms of the policy and political responses generated by the centre's SEZ framework.

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<sup>41</sup><http://kiadb.kar.nic.in/tender.htm>, accessed on 25 September 2006.

# Government Re-vision of the SEZ Policy

The central and state governments responded to the increasingly politicized environment surrounding the SEZ policy in a number of ways. The first was perhaps the most predictable: each abjured responsibility and blamed the other. Ministries of the central government claimed that they had framed the policy, but that it was up to states to implement it responsibly. State governments argued that they had received insufficient guidance from the center, and were being unfairly victimized by opportunistic politicians looking to fish in troubled waters.

These claims and counter-claims notwithstanding, as the complaints surrounding both policy and implementation mounted, the central government was forced to reverse its initial position, which was that the SEZ Rules should not be revised for a period of two years. The rationale for non-revision had been that stable expectations were needed if investors were to feel confident enough to commit the financial resources necessary to establish an initial wave of SEZs. The political logic soon overtook this stance.

Broadly speaking, there have been three rounds of revisions to the initial set of SEZ Rules, first framed in February 2006. These have come roughly every six months. In each round of revision, there have been both formal amendments to the SEZ Rules and less formal announcements of policy direction, the latter coming primarily from the so-called Empowered Group of Ministers (EGoM). The EGoM was established, under the chairmanship of Pranab Mukherjee, in mid 2006. The initial impetus was the 'success' of the policy, measured in terms of the rate at which SEZs were being approved. But more significant,

in terms of inter-departmental politics, were complaints from the Finance Ministry that their two representatives on the BoA <sup>42</sup> were being consistently overruled when they voiced objections based on their assessments of the revenue implications of proposed SEZs.

Other issues that over time required clarification included the ability of existing businesses (operating in the Domestic Tariff Area) to shift their operations into an SEZ, using existing machinery and equipment; the creation of a regulator who would determine the extent of newly created SEZ infrastructure to be exempted from tax on profits; and the area allowed for non-processing related activities (i.e., housing estates, commercial developments, schools and hospitals, leisure facilities). The EGoM reached compromise decisions on a number of matters, and developed procedural reforms to deal with others, in effect allowing greater input from throughout the bureaucracy on approvals as well as other, post-approval, decision-making. <sup>43</sup> One implication was that many decisions ended up requiring increased refereeing by the PMO.

The second set of amendments were issued in March 2007. These were notified just two days after the deaths stemming from the Nandigram protests, but had been the subject of deliberation since well before then. The government had begun to have serious doubts about the capacity of states to implement the land-acquisition portion of the SEZ policy without generating a backlash that would tarnish the entire effort. It therefore temporarily halted the process of approving new SEZs while the EGoM examined a range of issues. Within weeks of putting the approval process on hold, however, the BoA had resumed considering and clearing SEZ applications. Even observers who were otherwise supportive of the SEZ concept in principle (recognizing its value both in economic terms and as a means of adapting to a challenging political environment) considered the government to be acting in undue haste. The *Economic and Political Weekly* called the changes to the SEZ guidelines ‘piecemeal tinkering.’ <sup>44</sup> The *EPW* also pointed out that the government had still not instituted ‘a legally enforceable re-settlement and rehabilitation’ policy

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<sup>42</sup>One each from the Central Board of Direct Taxes and the Central Board of Excise and Customs.

<sup>43</sup>‘Zone Of Contention,’ *Business World*, 15 May 2006; and personal communication from a consultant to the finance ministry, 29 December 2006.

<sup>44</sup>‘Piecemeal Tinkering,’ *Economic and Political Weekly*, 21 April 2007, pp. 1399–1400.



that would hold SEZ promoters accountable for non-fulfillment of any such terms.

At least two of the changes announced during this period were substantial. First, one provision in the government order issued on 16 March 2007 appeared to accord the Board of Approvals wide latitude in changing the classification of land in an SEZ. Second, in early April 2007 the EGoM decided to prohibit the involvement of state governments in the acquisition of land for SEZ projects. An *EPW* editorial portrayed this as 'leaving peasants and landowners at the mercy of market forces', though many farmers no doubt would have preferred a voluntary transaction in the market to a compulsory sale engineered by corrupt officials acting at the behest of even more corrupt politicians. The *EPW* was on firmer ground when it claimed that the government was continuing 'to pander to the whims of SEZ promoters/developers'. One way it did this, in fact, was by allowing state governments *indirectly* to assist SEZ developers in buying land from landowners at below-market prices — not, in this case, through the Land Acquisition Act, but as mentioned in the previous section of this essay, by employing various tactics of intimidation. The government's soft spot for the SEZ developers was also indicated by the PMO's decision to ask the EGoM to review the Reserve Bank of India's September 2006 decision to classify bank financing of certain SEZ projects as equivalent to real-estate lending, which attracts higher interest rates (i.e., risk premia) than infrastructure projects.<sup>45</sup>

The government, eager to at least be seen to be addressing the rising political discontent, took other largely cosmetic changes in early 2007. It reduced the proportion of land within an SEZ that could be used for non-processing activities — from 65 percent down to 50 percent. This was widely considered still far too generous to promoters who were using the SEZ policy to subsidize the creation of mixed-use commercial developments — including housing, retail, and leisure complexes — with export-promotion little more than an afterthought. The other high-profile policy change, transparently devised to provide the appearance of getting tough on developers, was to set a ceiling of 5000 hectares on 'multi-product' SEZs. Not only was this sidestepping the main size issue — the proliferation of tiny SEZs that provided

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<sup>45</sup>Confederation of Indian Industry, *Exim News*, vol. 2, no. 3 (March 2007), p.10.

easy access to tax shelters but little by way of world-class infrastructure — it also made no sense in the context of the centre's decision to ban state-governments from compulsorily acquiring land for private promoters. If land was to be acquired through sales in the open market, why should it matter how large the SEZs were? Observers began to suspect that the ban on land-acquisition would not last long.

It now seems that, with the passing of another six months, the ban is indeed being partially lifted. (In at least some states, state land-acquisition processes never ceased anyway: surveys and negotiations continued, even if the issuance of acquisition notifications did not.) This third set of SEZ policy changes has not yet been officially gazetted, but was unofficially agreed by the EGoM at the end of August 2007.<sup>46</sup> It includes a provision that allows states to acquire land compulsorily for SEZ projects, but only up to a maximum of 30 percent of the total project area. If private developers are able to acquire 70 percent of the land themselves, the state government would be permitted to acquire the rest via the procedures set forth in the Land Acquisition Act. The government also reportedly considered, but did not act upon, a proposal to prohibit the transfer of compulsorily acquired land to private developers; the alternative is to offer the land on long-term leases.

State governments in many cases have revisited their policy frameworks, and have revised the procedures and standards used in implementing the SEZ policy. Returned to the Chief Ministership of Uttar Pradesh in 2007, Mayawati wasted little time before announcing that the state would be framing and implementing a new set of norms — partly in response to changes announced in the central guidelines and partly on the basis of what was perceived to be in the best interests of the state. The first substantive action taken in this connection was to put on indefinite hold the plans of the Anil Ambani group to construct an SEZ in Noida. As approximately 2000 acres of land for the proposed SEZ still needed to be obtained, and farmers were objecting to the forced sale of land, the government claimed that it was left with no option but to reject Ambani's proposal. The state government claimed merely to be following the recommendation of the committee established under the industrial development commissioner, which included proposals to tighten tax-exemptions

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<sup>46</sup>'Agri Growth Central to Overall Prosperity', *Economic Times*, 5 September 2007.

in non-processing areas of SEZs and to ensure that that stamp-duty remission would thenceforth take place only at the time of initial registration.<sup>47</sup> No one close to UP politics was in any doubt, however, that the decision on the Noida SEZ was driven largely by Mr Ambani's political proximity to the Samajwadi Party. This reinforced the impression that, if (as often claimed by beleaguered chief ministers) opposition-party support for anti-SEZ protestors was opportunistic, then the actions of state governments could be equally so.

Other state governments took steps to revise their policy frameworks, particularly with respect to the permitted size of SEZs, the nature of tax concessions and the conditions imposed thereon, the sectors that would receive priority in approvals for proposed SEZs, the type and location of land available for acquisition, the procedures through which acquisition could take place, the forms and levels of compensation payable to those from whom land was compulsorily acquired, and many other matters. Notable among the states where governments felt compelled to at least be seen to be taking a fresh look at their SEZ policies were Haryana, Maharashtra, Orissa, and West Bengal. These were also, not incidentally, the states where some of the most visible and sustained protests took place.

The constant revision of the SEZ policy should not be mistaken for responsive governance. It is mainly a consequence of an ill-considered policy initiative that has generated considerable political resistance. Moreover, the frequency of SEZ policy iteration gives rise to rent seeking. It provides incentives for private actors to seek to influence each successive round of policy revision, or at the very least to purchase inside information in advance of key decisions being formally announced. The frequent policy changes also create ambiguities that provide bureaucrats greater scope to exercise discretion: officials are able to cover their tracks when non-compliant decisions are exposed by invoking the excuse that the operative policy was a matter of interpretation given ambiguous and competing policy directives. The awareness that liberalizing policies which appear to reduce the scope for discretion will, over time, be subjected to iteration — and therefore regular opportunities for rent-seeking — is one of the reasons why there is not more resistance within

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<sup>47</sup> 'Anil Ambani's SEZ in Noida, Not Possible Now', *The Tribune* (Chandigarh), 20 August, 2007.

## GOVERNMENT RE-VISION OF THE SEZ POLICY

the bureaucracy to the shift toward a more liberal policy regime. For the astute and well-networked official, the state of 'permanent reform' is conducive to the generation of illicit income.

# Implications: Taking Stock of the Politics of SEZs

Looking back at the pattern to have emerged in the formulation of the SEZ policy, the specification of its content, the calculations concerning its political feasibility, the resistance that arose in the process of implementation, and the subsequent attempts at policy revision (both *de jure* and *de facto*), three arguments can be advanced.

The first is that India's reform effort may have reached the limits of what can be achieved through shrewd political management of the policy process. Partisan blame-shifting, institutional burden-spreading, reverse forum-shopping, the purposeful division of adversely affected constituencies, careful policy sequencing — these and other techniques for reducing political resistance (including some that rely on systematic illegality) have over the past decade and a half been important contributors to India's ability gradually to transform its economic framework. But this strategic paradigm, which involves the manipulation of incentives and disrupting the tactical calculus of key interest groups and individual elites is increasingly unviable as a means of continuing the process of reform.

The chief irony to have emerged after approximately three years of SEZ policy formulation, implementation, and revision is that an approach designed to effect an end run around the legal and political obstacles to furthering India's reform agenda has ended up generating not only a potentially serious backlash against the SEZ policy, but a sense of disenchantment about the state's approach to economic reform more generally — in particular its lack of attention to the agricultural sector and its disregard of the rural poor.

## IMPLICATIONS: TAKING STOCK OF THE POLITICS OF SEZs

India's SEZ policy has created an extremely potent symbol around which opponents of liberalization — from grassroots activists to national party leaders — have been able to rally. Indeed, one would be hard pressed to imagine a single action more likely to unite the various anti-reform groups that have for so long been fighting dispersed battles on a variety of lonely fronts. Had a committee of anti-reform forces been constituted to devise such a policy measure, the implementation of which could catalyze a wave of political discontent, recommending the passage of the SEZ Act would not have been a bad choice. SEZs have brought economic reform firmly into the domain of mass politics.

The SEZ policy is an attempt to build economic infrastructure and regulatory capacity within small spaces when it is deemed politically unfeasible to do so on a national scale. Politicians in the UPA were not unreasonable to believe that the nature of the policy, and the decentralized means by which it would take concrete shape, would erect barriers to political resistance. As it happens, this approach has fueled widespread political discontent. Protest that initially seemed sporadic and dispersed among far-flung sites (manageable by local officials and state governments) has coalesced into a pattern of opposition to reform that has cast the SEZ policy as the poster-child for uncaring globalization.

Over time, complaints about SEZ implementation became so widespread, and the land-acquisition abuses followed such a predictable pattern, that the central government's response — that problems were the result of faulty actions taken by state governments — began to ring hollow. The conceptual firewall between policy and implementation was revealed as spurious: if implementation could be so consistently abusive, then there must be something wrong with the policy framework. The defenses against political blame were proving less robust than the centre's political strategists had hoped, and their faith in the political management capacities of states was appearing decidedly misplaced.

The second argument is closely related to the first. The political troubles that the SEZ policy has encountered underscores one of the costs of corruption that has tended to be overlooked in existing debates. Corruption is typically seen as exacting a cost in terms of various measures of efficiency — for instance, by increasing transaction costs and creating incentives for particularly

destructive varieties of rent-seeking behaviour.<sup>48</sup> More recently, an understanding of the costs of corruption in terms of equity have been highlighted, and have indeed spurred on forms of anti-corruption activism that seek to reduce the effects of corruption on the poor.<sup>49</sup>

But it has become increasingly obvious that it is the interaction between efficiency and equity-depleting forms of corruption that is particularly damaging. How? Attempts by governments to mitigate the effects of corruption on segments of the population that have not benefited from liberalization — the rural poor in particular — have often been foiled by a siphoning of funds by corrupt officials and other middlemen. This is bad in its own right, but is particularly damaging to the state's ability to build the political consensus required to press ahead with a reform agenda that seeks to reduce structural inefficiencies in the operation of the economy. In other words, politically speaking, corruption that hurts the poor not only undermines equity, it can also harm the prospects for the creation of a more efficient economy.<sup>50</sup>

It is for this reason that the accountability and social-audit provisions of the NREGA are so important (and why they were given such prominence): this program is the flagship of the UPA's effort to make peace with the rural poor, which might otherwise vent its dissatisfaction with elite-oriented reform against this government, just as it did the last one. Even more worrying precedents for the UPA are the cases of two state governments — Digvijay Singh's in Madhya Pradesh and Ashok Gehlot's in Rajasthan — that were thrown out of office by discontented electorates in late 2003 *despite* the attempts of both governments to improve conditions for the rural poor. A dispassionate interpretation of these two electoral outcomes would have to fault corruption in the programs through which the respective state governments sought to build support among poorer voters.

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<sup>48</sup>Paulo Mauro, 'The Effects of Corruption on Growth, Investment, and Government Expenditure', *IMF Working Paper WP/96/98* (Washington D.C.: International Monetary Fund, 1996).

<sup>49</sup>Rob Jenkins and Anne Marie Goetz, 'Bias and Capture: Corruption, Poverty and the Limits of Civil Society in India', in Marc Blecher and Robert Benewick (eds), *Asian Politics in Development* (London: Frank Cass, 2003), pp. 109–22.

<sup>50</sup>Rob Jenkins, 'Democracy, Development and India's Struggle Against Corruption', *Public Policy Research*, vol. 13, no. 3 (Sept-Dec 2006), pp. 155–163.

## IMPLICATIONS: TAKING STOCK OF THE POLITICS OF SEZs

This syndrome (of corruption as a constraint on the ability to buy the political support that risk-taking governments desperately need) is directly relevant to the fate of India's SEZ policy. In response to the many 'implementation problems' that have arisen in the SEZ policy — the charges of systematic bias, the widespread and persistent political protests — many recommendations have been put forward about how grassroots opposition to the policy among affected groups could be overcome. One business school professor, citing the Chinese case, advocates a 'well-designed' 'compensation' package for farmers whose land is acquired.<sup>51</sup> (That an authoritarian government's approach to displaced agriculturists is considered a model of humane treatment compared to what has been happening in India provides some indication of how badly India's policymakers have thus far handled this issue.). This kind of compensation package — which resembles proposals floated in various think tanks as well as in the Planning Commission — would include 'monetary' (payment for land) and 'non-monetary' components, the latter including jobs, housing, and subsidized healthcare and education.

A compensation-oriented approach to the SEZ policy's land-acquisition problems would, however, face huge obstacles. Chief among these is the sheer lack of confidence among ordinary people that whatever compensations are promised will be forthcoming — or that benefits will reach the intended beneficiaries. This is not uniformly true across all classes of people, or all Indian states, or all regions within states. But a lack of confidence in the government's ability to deliver on its promises — which is to say, the state's severely dented credibility — poses formidable difficulties.

Take the case of the large SEZ projects being planned in and around Mumbai. Several very reputable NGOs working in the city report abuses that conform to an extremely disturbing pattern. At least 50 cases of forged signatures to obtain land have been lodged (there is no way to determine how many are legitimate complaints). One activist made the point that promises of employment were particularly suspect in the eyes of residents.<sup>52</sup> Pledges from SEZ promoters as well as the state government come in the wake of earlier

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<sup>51</sup>'Sizing Up the SEZ Potential', *Indian Express*, 31 August 2007.

<sup>52</sup>Personal Communication, 12 August 2007; see also <http://sify.com/finance/fullstory.php?id=14521321>



rounds of broken promises with respect to land acquisition. In mid 2006 both Sonia Gandhi and Agriculture Minister Sharad Pawar had announced that fertile agricultural land would not be acquired for SEZs. Yet in Maharashtra the state government continued acquiring such land for a large SEZ project in Raigad district. Farmers just outside Mumbai were served with acquisition notices for a combined 28,000 hectares for this SEZ.

The dispute over broken promises in this case, as in others, hinges on the distinction between productive and unproductive land, which are sometimes referred to as 'fertile' and 'infertile' land. Most impartial observers will say that much of the land classified as 'barren' is perfectly productive — some of it in practice, most of it potentially. Farmers who have been resisting land acquisition explicitly referred to earlier episodes where landowners were treated unfairly; the land acquisition process for the Ispat Denro plant in Raigad and the IPCL plan at Nagothane loomed large in these accounts.<sup>53</sup> It is the memory of these earlier betrayals that, according to spokespeople from activists groups such as Ekvira Jameen Bachao Andolan, helps to explain the rallies of up to 30,000 protestors that have taken place in Pune and elsewhere.

The Maharashtra Industrial Development Corporation (MIDC), like similar agencies in other states, has sought to assure landowners that they will be assigned plots in the SEZs in which the MIDC is an equity partner. The MIDC has also promised assistance in setting up business units in adjacent areas likely to undergo rapid development. But given the dismal record of the Maharashtra government in fulfilling its various promises, is it any wonder that landowners are not convinced by the assurances offered by MIDC? It is not that farmers are clinging to land out of some atavistic attachment to real property; they have a rational belief, based on experience, that promises will not be kept.

In short, the credibility of the Indian state as a broker of effective compromises on a large scale is so damaged by its repeated failures to stem corruption among the frontline bureaucracies that would be charged with delivering compensation packages, that proposals based on compensation find few takers and become unviable as deadlock-breaking solutions. This is a pathological condition for a political system that must rely on such accommodations to

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<sup>53</sup>'Rural Resistance', *Frontline*, 7 October 2006.

## IMPLICATIONS: TAKING STOCK OF THE POLITICS OF SEZs

bring about desired policy changes.

Some suggest that private-sector firms will be better placed to develop compensation packages that landowners will find attractive. Private firms may have image problems, but the kinds of compensation offered would be more direct, and backed by specific contracts for individuals rather than revocable policy commitments for classes of landowners, it is argued. (There are several efforts by private-sector firms to forge direct links with landowners: for instance, textile firms in Bangalore seeking to establish a sector-specific SEZ have promised to assist farmers with impartial advice on the process of selling their land, and to put them in touch with financial advisors on how to invest the proceeds of such sales.) The shortcoming of this argument is that the contracts signed between firms and individual landowners would similarly rely on the enforcement machinery of the state, including a grotesquely corrupt legal system. The corruption of the Indian state, in short, undermines the confidence required on the part of people with which the state would like to enter into contracts, which if concluded could help to buy the political peace necessary to deepen economic reform.

One example of how bad policy design undermines confidence in the *state-as-broker* concerns the timing of land contracts and SEZ approvals. When firms buy land directly from owners, the agreements typically specify that the transaction will only be consummated with each individual seller once the company has amassed agreements in principle to buy the aggregate amount of land needed for the SEZ to go ahead. This would be unproblematic if there was a definite deadline for amassing the land (and finance and other necessary elements) after which the agreement would lapse. But because in some purchase agreements no deadline has been stipulated, this has allowed firms to, in effect, tie up in a contingent contract land owned by people who find that their main asset is legally encumbered. This problem has been pointed out to farmers by bankers who transact business with them on other matters, as well as by opposition politicians who seek to convince farmers that they have been given a raw deal. That government rules have allowed what amounts to a relatively one-sided option contract to continue has further raised suspicions among the public. This further erodes the trust necessary to forge compensatory policy

frameworks.<sup>54</sup>

Recent government efforts to arrive at a policy compromise on the land issues related to SEZ development are, if anything, likely to generate even further suspicion. The 70:30 policy on land acquisition — which allows state governments to acquire 30 percent of the land for an SEZ compulsorily if the promoter is able to acquire the other 70 percent through private-market transactions — will in fact enhance the negotiating leverage of SEZ land-seekers by considerably more than 30 percent. Thanks to this new policy, a landowner who is approached by an SEZ developer wishing to purchase his land, but who is reluctant to sell, will be presented with the unattractive possibility of ending up as part of the 30 percent whose land is compulsorily acquired by the state government on the developer's behalf. Developers will attempt to convey the impression to *all* potential sellers that they (the developers) are close to meeting the 70 percent threshold. This increases the pressure on landowners to sell to the developer — at what the developer will claim is a good price — out of fear that the alternative (i.e., what the state government will pay) will be substantially less. Landowners will want to be part of the 'lucky' 70, rather than the unfortunate 30. Simply the threat of being subjected to compulsory purchase — through a state land-acquisition process that is known to be corrupt, inefficient, and unreliable — will exert a downward pressure on the prices available to private landowners. Industry analysts, not surprisingly, have welcomed the new policy as it will ensure that 'projects will not be held to ransom' by recalcitrant landowners.<sup>55</sup>

This 70:30 policy 'compromise' was bundled with a draft 'resettlement and rehabilitation' policy. But the failure of India's state governments to implement even Supreme Court-ordered resettlement and rehabilitation policies for people displaced by large-scale *public*-sector development projects — notably the Narmada Dam — has, not surprisingly, made landowners dismissive of promises issued under the revised SEZ policy.

Farmers, it should be added, are naturally suspicious of promises made by

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<sup>54</sup>This summary emerged from the author's interview with an analyst in a major US financial institution that has large investments in India, at the Bear Stearns 'Global India' conference, New York, 5 August 2006.

<sup>55</sup>These were the words of a senior manager at PricewaterhouseCoopers. 'Rehab Policy Good News for SEZs', *Business Standard*, 1 September 2007.

a state that has done little to improve the conditions facing agriculture — a state that has in effect created the push factors that cause many to consider selling their land their only option. As Narendar Pani has written, encouraging people to make the shift out of agriculture means ‘providing them economic opportunities that are consistent with a modern economy,’ requiring substantial and well-funded ‘initiatives ranging from education to incubators that allow entrepreneurship to mature.’ These cannot be future promises. ‘As the protests over land acquisition grow across the country state governments that want to avoid social turmoil will have to recognize that people have to be drawn out of agriculture before their land is acquired and not the other way round.’<sup>56</sup>

The third argument to emerge from the SEZ story relates most directly to this workshop’s desire to explore connections between the various dimensions of India’s ‘great transformation’. Is there any link between India’s experience with SEZ policy to date and what has been called India’s ‘second democratic upsurge’? Arguably the most direct connection is of a negative variety: the concerns about unaccountable governance within SEZs, outlined in Section IV of the paper, would seem to paint a grim picture of what India’s economic modernizers consider necessary to ensure its continued prosperity. If SEZs are a harbinger of what is to come, the democratic gains realized for historically oppressed groups through one set of institutions could well be reversed through others. The common worry that democratic principles will be sacrificed in the operation of SEZs — just as they have been in the process of establishing them — is certainly not without merit. If nothing else, the lack of precision regarding the applicable legal regime within SEZs on many economic and non-economic matters is a matter of serious concern. That certain categories of rights will receive short shrift, either by law or as a matter of practice, is all too easy to imagine. In particular, there is justifiable anxiety about the legal provisions under which labour will be regulated — the full gamut of issues including hiring practices, security of employment, wage and pension entitlements, occupational health and safety, the ability to unionize, rights to collective bargaining, and the mechanisms for resolving individual and class-action disputes.

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<sup>56</sup>*Economic Times*, 11 Dec 2006

## THE POLITICS OF INDIA'S SPECIAL ECONOMIC ZONES

These legitimate worries notwithstanding, there is a sense in which the emphasis of this line of criticism — in which, it is feared, the occupants of SEZs will be offered a second-rate version of democratic governance — may miss the significance of what is taking place. In particular, critics who stress the democratic deficit seemingly built into the SEZ model of governance may have misread the relationship between the governance of SEZs and the continued democratization of India's democracy.

Without doubt, the promoters of SEZs and the businesses that will operate within them seek to evade the burdensome regulations (and time-consuming procedural requirements) of India's democratically constituted state. But, arguably, so do many of the people who will flock to the SEZs. A good proportion of those who will reside in SEZs, or who will aspire to do so, will be members of India's middle class. It is for technological and managerial professionals that the extensive 'social amenities' are being constructed — not only housing developments, but a huge array of retail and leisure facilities designed to attract upwardly mobile members of Indian society. These zones of relative affluence will offer not merely economic privileges, but in a sense a form of desirable political exile as well.

In other words, the idea of the multipurpose SEZ, where large numbers of people will reside as well as work, is premised on a belief that a substantial segment of India's middle class is eager to escape from India's democracy as currently constituted. SEZs provide a means for a privileged (but growing) segment of India's polity to avoid the tumult that characterizes contemporary India, both the politicization of religious identity and the second democratic upsurge. It is worth noting that this longing to escape the messy reality of politics may well be attractive even for people attracted to Hindu nationalism as a form of political expression, or people from the very social groups whose political ascendancy constitutes the recent democratic upsurge.

This does not imply that future residents of SEZs will not ideally desire the protection of law, or the political voice that comes from representative government. They are, however, likely to be price-conscious consumers of democracy. There are a great many upwardly mobile, professionally qualified, globally connected people who consider India's form of politics too chaotic (and indeed corrupt) to deliver the benefits classically associated with democracy. The entry into mainstream politics of previously marginalized groups — people

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regarded, even by first-generation members of the middle class, as socially backward, easily manipulated by populist demagogues, and too often willing to sacrifice progress at the altar of equality — has for India's emerging elite made living amidst India's current democratic dispensation an unattractive proposition. SEZs offer a form of partial political secession — in the same way that access to privatized health and education services allows better-off people to opt out of (and therefore further impoverish) public provision. Moving to an offshore haven located onshore may thus constitute the next best thing to emigrating abroad — better, in fact, because of the ability to do so while remaining in India. If forfeiting some of the procedural benefits of democracy is the price of admission, this is a cost that many Indians may well be willing to pay.

As SEZs move from the drawing board to construction to full operation, it may well be that we will witness a shift of emphasis among those who currently criticize SEZs as likely enclaves of undemocratic governance. If even a modest number of SEZs succeed in generating more entrepreneurial activity, creating high-paying jobs, building quality business and social infrastructure, and providing a zone of efficient (if less than fully representative) governance, they may end up serving an even more sinister purpose than critics currently fear. Rather than ending up as Dickensian dystopias, SEZs may well serve as a showcase for the merits of a more authoritarian form of governance. This is perhaps the most disturbing aspect of these special governance zones. It is not difficult to imagine political leaders making the case that India's decentralized, representation-obsessed, procedure-encumbered, judicially-reviewed form of democracy had become unworkable — and that its SEZs had demonstrated on a small scale what the rest of the country should adopt on a nationwide basis: a streamlined version of governance in which officials and business elites collaborate to provide effective public services in the context of a long-term vision of India's economic place in the world. A kind of South Korea in South Asia.

As for the third dimension of India's great transformation — the rise of Hindu nationalism as a political force — there is perhaps less of a direct thematic linkage. Still, it is notable that when defending SEZs as necessary, some BJP politicians have spoken of their role in helping to project India's economic power. SEZs, according to this view, are a means of preparing

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India's firms for operating within the foreign environments in which they increasingly will have to do business — that is, in the global markets and overseas jurisdictions where Indian capital's urge for expansion is inevitably taking them.

At least one BJP spokesperson has also advanced the argument that SEZs would be good for the preservation of the (presumably Hindu) nation by providing an alternative to the emigration of India's skilled professionals.<sup>57</sup> The implication, of course, is that India is creating its own 'abroad' within its borders — a hybridized space that can serve as a functional equivalent of foreign territory. So rather than SEZs being seen as scars on the nation's sacred geography, they can be regarded as a symbolic absorption of the world beyond India. Moreover, SEZs may even help to shield the core of India from what some Hindu nationalists (and others) decry as the corrupting foreign influences of consumerism and western lifestyles by quarantining these things, to the degree possible, within defined enclaves where they can do less harm.

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<sup>57</sup>'SEZs Good, but Keep off Farm Lands, Says BJP,' UNI, 10 October 2006.

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